United States Court of Appeals

for the Second Circuit

APPELLANT'S BRIEF & APPENDIX

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74-2280

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IN THE

United States Court of Appeals

FOR THE SECOND CIRCUIT

Docket No. 74-2280

COLONIAL REALTY CORPORATION,

Plaintiff-Appellant,

—against—

JOHN MacWILLIAMS, JR., JAMES E. BRENNAN and COLONIAL PENN GROUP, INC.,

Defendants-Appellees.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK

BRIEF FOR PLAINTIFF-APPELLANT
and
JOINT APPENDIX

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Dated: December 9, 1974

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TABLE OF CONTENTS

TABLE OF CASES

STATUTES AND REGULATIONS

AUTHORITIES

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BRIEF FOR PLAINTIFF-APPELLANT

In this action to recover alleged short-swing profits of defendants pursuant to § 16(b) of the Securities Exchange Act of 1934 (the "Act"), plaintiff appeals from an order of the District Court for Southern New York, Gurfein, J., dismissing the complaint for legal insufficiency. The decision below (A-6) is reported at 381 F. Supp. 26.

The text of § 16(a) and (b) of the Act, 15 USC § 78p(a) and (b), is set forth in the Addendum, p. 29 below. The statute renders a corporate director or officer liable for any profit he realizes from a purchase and sale, or a sale and purchase, of an equity security of his corporation "within any period of less than six months." This appeal turns on the effect to be given the quoted phrase.

QUESTION PRESENTED

Is a corporate cfficer or director liable under § 16(b) of the Exchange Act for the profits he derives from purchasing his company's stock six months minus a day after selling the same stock?

STATEMENT OF THE CASE

The order below was entered September 11, 1974 (A-9). Plaintiff filed its notice of appeal on September 19, 1974 (i). This Court's jurisdiction rests on 28 USC § 1291. The District Court's jurisdiction rested on § 27 of the Act (A-1).

The complaint alleges that plaintiff is a stockholder of defendant Colonial Penn Group, Inc. (the "Corporation"). Defendants MacWilliams and Brennan are officers of the Corporation. The Corporation's common stock is registered pursuant to § 12 of the Act (A-1, A-2).

Defendant MacWilliams sold 50,000 common shares of the Corporation on December 20, 1972 and purchased 45,000 shares on June 19, 1973. Defendant Brennan sold 4,000 common shares on December 22, 1972 and purchased 5,000 shares on June 21, 1973. Both MacWilliams and Brennan realized substantial profits from their transactions. When plaintiff's demand that the Corporation sue for these profits remained unsatisfied for more than two months, plaintiff brought this action on behalf of the Corporation on April 25, 1974 (A-2, A-3).

MacWilliams and Brennan moved, without affidavit, to dismiss the complaint for failure to state a claim, on the theory that the transactions complained of did not occur within the statutory period of less than six months (A-5).

Judge Gurfein granted the motion (A-6), feeling "constrained" to do so (A-8) by what he considered the stare decisis effect of a dictum in Stella v. Graham-Paige Motors Corp., 132 F. Supp. 100, 103-106 (S.D.N.Y. 1955, Dimock, J.), remanded, 232 F. 2d 299 (2d Cir.), cert. denied, 352 U.S. 831 (1956).

THE ISSUES

1. In the Stella case, Judge Dimock interpreted § 16(b) as prescribing a holding period of six months minus two days. Customarily, of course, a time period running from a designated event is computed by excluding the day of the event and including the last day of the period (pp. 8 et seq., below). Judge Dimock adopted the inverse method of computation. He thought that the day of the initial securities transaction must be included in the six months because, under the language of the statute, purchase and sale must occur "within" the period. In addition, Judge Dimock lopped off a full day at the end of the six months because the statutory period is "less than six months" and the law does

ke into account fractions of a day. In this fashion, uced the six months by two days, taking off one day beginning and one at the end of the period.

By adopting this procedure, the Court below ated the present defendants from liability although epurchased the Corporation's stock six months minus after they had sold it.

We propose to show that the District Court erred counts: The day of the initial transaction should uded from the six months, whereas the last day of months should be included therein. If we be right her of these points, then defendants' transactions thin the statutory period.

2. In the factual context of the Stella case, imock's discussion was pure dictum, immaterial to come. The securities purchase in Stella occurred uary 10, 1947; the corresponding sales occurred on ore August 7. It made, therefore, no difference

whether the last day of the statutory period was August 8 (as Judge Dimock held, 132 F. Supp. at 106) or one or two days later.

Nor did this Court's decision in Stella approve Judge Dimock's computation (as Judge Gurfein thought it did). This Court stated (232 F. 2d at 301):

> "We agree with the trial judge that the purchase of the stock occurred on February 10, 1947, and that therefore sales made before August 8, 1947 were within the statutory period." (Emphasis added)

As noted, the statutory period computed according to Judge Dimock's method included August 8. Accordingly, sales made on August 8 would have been within the statutory period. This Court, however, was concerned only with the sales actually made, all of which were before August 8 and were, therefore, within the statutory period, no matter how computed. This Court thus had no occasion to approve or disapprove Judge Dimock's computation and did not purport to do so.

The District Court's dictum in Stella, unreviewed by this Court, has no force to bind this Court as a precedent or as stare decisis. Calaf v. Gonzalez, 127 F. 2d 934, 938 (1st Cir. 1942); McIlhenny Co. v. Gaidry, 253 F. 613, 615 (5th Cir. 1918). On the appellate level, the proper computation of the holding period of § 16(b) is, therefore, still an open question.*

*The Court below thought it of some significance that neither Congress nor the SEC has acted in response to the Stella dictum (A-8, n.1). It would be highly unrealistic to "expect Congress to make an affirmative move every time a lower court indulges in an erroneous interpretation [of a statute];" Jones v. Liberty Glass Co., 332 U.S. 524, 534 (1947). Even in overruling its own decisions, the Supreme Court deems it "at best treacherous to find in congressional silence alone the adoption of a controlling rule of law.*** the mere silence of Congress is not a sufficient reason for refusing to reconsider the decision;" Boys Markets v. Retail Clerks Union, 398 U.S. 235. 241-42 (1970); NLRB v. Plasterers' Local Union, 404 U.S. 116, 129-30 (1971).

POINT I

THE HOLDING PERIOD OF § 16(b) RUNS FROM THE INITIAL SECURITIES PURCHASE OR SALE TO AND INCLUDING THE CORRESPONDING DATE SIX MONTHS LATER

Defendant MacWilliams sold the Corporation's stock on December 20, 1972. The corresponding date six months later was June 20, 1973. This, we submit, was the last day of the statutory period. Any purchase on or before June 20 rendered MacWilliams liable for his profits. Since he did repurchase the Corporation's stock on June 19, liability attached, with one day to spare.*

Our position rests on two propositions. (1) The date of the initial purchase or sale - here, December 20, 1972 - must be excluded from the statutory period. (2) The last day of the six months - here, June 20, 1973 - must be included in the statutory period. We shall show that

*The same observation applies to defendant Brennan, who sold on December 22, 1972 and repurchased on June 21, 1973.

elementary rules of statutory interpretation, the purpose of § 16(b), its legislative history, and the overwhelming weight of its construction by the courts and by the Securities and Exchange Commission, support these propositions.

A. The date of the initial purchase is excluded from the statutory period.

1. Few rules of law are better known or more firmly settled than the maxim that, in computing a time period beginning at a specified event, the day of that event is excluded. The most familiar formulation is that by Mr. Justice Holmes in Burnet v. Willingham Loan & Trust Co., 282 U.S. 437, 439 (1931):

> "The general rule was laid down long ago in language quoted from Chief Justice Bronson, Cornell v. Moulton, 3 Denio, 12: 'When the period allowed for doing an act is to be reckoned from the making of a contract, or the happening of any other event, the day on which the event happened may be regarded as an entirety, or a point of time; and so may be excluded from the computation.'"

In the Burnet case a statute permitted a tax assessment to be made "within four years after the return was filed." The taxpayer filed his return on March 15, 1922: the assessment was made on March 15, 1926. The Supreme Court held that it was timely.

A veritable host of cases, from ancient vintage to recent authority, confirms and applies the Burnet rule, e.g., Sheets v. Selden's Lessee, 2 Wall. (69 U.S.) 177, 190 (1865); United States v. Schwenoha, 383 F. 2d 395, 396 (2d Cir. 1967), cert. denied, 390 U.S. 904 (1968); Becker v. C.I.R., 378 F. 2d 767, 769 (3d Cir. 1967); Fogel v. C.I.R., 203 F.2d 347, 349 (5th Cir. 1953); United States v. Hardy, 74 F. 2d 841, 842 (4th Cir. 1935). The rule has been expressly adopted by the Bankruptcy Act, the Federal Rules* and other statutes.

The statutory holding period prescribed by § 16(b) begins with the initial purchase (or sale) of secur-

*Section 31 of the Bankruptcy Act, 11 USC § 54 ; Rule 6(a) FRCP.

ties. The day of the initial purchase (or sale) is, therefore, excluded.

2. Judge Dimock, in Stella, thought otherwise (132 F. Supp. at 104). He reasoned that, in cases like Burnet, supra, the time period was to be computed "from" or "after" a given event; whereas under § 16(b) the purchase and sale must occur "within" the statutory period. He considered it a "contradiction in terms" to treat the initial purchase as being "within" a period that did not start to run until after the purchase.

Judge Dimock's error lay in treating a legal fiction as if it had to reflect reality. The Burnet rule rests on a legal fiction. Take a statutory period running "from" a given event; even if the event occurs, say, at 11 A.M., the period is reckoned only from the next following midnight. In the words of Justice Holmes, "the day on which the event happened may be regarded as * * * a point of time, and so may be excluded from the computation" (Burnet, 282 U.S. at 439). On Judge Dimock's reasoning,it would be

a "contradiction in terms" to let a period that runs "from" an event run from the midnight following the event; but it is the law that treats the day as a mere point of time and thus indulges the fiction that the event happened only at the next following midnight.

The same legal fiction governs the statutory period of § 16(b). The sale by defendant MacWilliams took place on December 20. The law treats it as happening at the next following midnight, i.e., at the first moment of December 21. The sale was thus "within" the six months' period whose first day was December 21. Here, as in every computation of time, the day of the event is not included in the computation.

Congress, in enacting § 16(b), could not have meant to ignore the Burnet rule. The case had been decided just three years before. Its rule was of ancient dignity and universal acceptance. Any intent to depart from it would have required clear and explicit statutory language. No such language is found in § 16(b).

B. The last day of the six months is included in the statutory period.

Under a rule no less elementary than that just discussed, the computation of a period of time includes the last day of the period. Sheets v. Selden's Lessee, supra, 2 Wall. (69 U.S.) 177, 190; Siegelschiffer v. Penn Mutual L. Ins. Co., 248 Fed. 226, 228 (2d Cir. 1917), mandamus denied, 246 U.S. 654 (1918); Becker v. C.I.R., supra, 378 F. 2d 767, 769 (3d Cir. 1967); Fogel v. C.I.R., supra, 203 F. 2d 347, 349 (5th Cir. 1953). A sale on the last day of the six months is, therefore, within the prohibition of § 16(b). The section, to be sure, prescribes a holding period of "less than six months"; but since the last day of the six months runs until midnight, Joint Council v. Delaware, L. & W. R. Co., 157 F. 2d 417, 420-21 (2nd Cir. 1946), a sale prior to midnight, i.e., during the course of the day, is indeed within "less than six months".

Again, Judge Dimock, in Stella, thought otherwise (132 F. Supp. at 104):

> "To be less than six months the statutory period must be six months minus one full period from midnight to midnight since the law does not take into account fractions of a day. 2 Bl. Com. 141."

It is true, of course, that, in appropriate circumstances, the law ignores fractions of a day, but "the rule is purely one of convenience", Louisville v. Portsmouth Saving Bank, 104 U.S. 469, 474-75 (1881), is subject to numerous exceptions, In re Gubelman, 10 F.2d 926, 930 (2d Cir. 1925), rev'd in other respects, 275 U.S. 254 (1927), and is intended for situations quite different from that here involved. Its purpose is simply "to avoid disputes" (2 Blackstone Com. 141, in the passage cited by Judge Dimock, supra) and to prevent a "minuteness of inquiry [which] would usually be attended with great difficulty, without conducing to a very satisfactory result", Cornell v. Moulton, 3 Den. (N.Y.) 12, 15 (1846) (a case cited by Justice Holmes in Burnet, supra, 282 U.S. at 439), since it would be "impracticable" to "require an accurate account to be kept of the exact hour, minute, and second of the occurrence

of the act to be timed;" Greulich v. Monnin, 142 Ohio St. 113, 117, 50 N.E. 2d 310, 312, 149 A.L.R. 477, 480 (1943). Hence it is that a time period that would otherwise start or terminate in the course of a day is deemed to start or terminate at the end of the day.

None of the reasons for ignoring fractions of a day is here applicable. The convenience of record keeping is the same whether the statutory period expires at the end of the last day of the six months or at the end of the last day but one. In no event is there a need to record the exact hour and minute of the securities sale; for whether that sale occurs at 10:00 A.M. or 4:00 P.M. of the last day of the six months, it is within "less than six months" from the initial purchase. The elimination of the last day of the six months would thus serve neither convenience nor any other purpose; and since the maxim treating days as indivisible is simply one of convenience, there is no room for its application here.

Neither Judge Dimock nor the present defendants have cited a single precedent applying the "indivisible day"

maxim to an act that must be done, or not done, within "less than" a given period. Such authorities as we have found compel the opposite conclusion.

Under the Internal Revenue Code, 26 USC § 1222, "The term 'long-term capital gain' means gain from the sale or exchange of a capital asset held for more than 6 months ***". Under Judge Dimock's rationale, a holding period of "more than 6 months" would mean six months plus one full day, on the theory that the law ignores fractions of a day. It is thoroughly settled, however, that a sale on the first day following expiration of the six months is entitled to long-term capital gain treatment. Becker v. C.I.R., supra, 378 F. 2d 767, 769 (3d Cir. 1967); Fogel v. C.I.R., supra, 203 F. 2d 347, 349 (5th Cir. 1953); Revenue Ruling 70-598, Cumul. Bull. 1970-2, p. 168; 3B Mertens, Federal Income Taxation, § 22.104, pp. 750-51 (Rev. Ed. 1973). The principle does not rest on any peculiarity of the tax laws but - as the authorities cited show - upon the general maxims governing the computation of periods of time.

Judge Gurfein thought that analogies drawn from unrelated areas of law are "at best of minimal impact" (A-8). We fail to see the reason. Judge Dimock (whom Judge Gurfein followed) placed his principal reliance on Blackstone (132 F. Supp. at 104), who certainly did not address his remarks to the Securities Exchange Act. The principles governing the computation of time are of general application so that, in the absence of clear distinguishing factors, precedents from one area of the law are valuable guides to others.

There can be no distinction in principle between periods of "more than six months" and "less than six months". A full six months plus one minute is "more than six months". A full six months minus one minute is "less than six months". The "indivisible day" maxim is inapplicable in either case. Judge Dimock erred, therefore, in eliminating the last day of the six months.

C. The context of § 16(b), its legislative history, and the authorities construing it indicate that Congress intended to prescribe a full six months' holding period.

Judge Gurfein thought that trimming a day or two off the statutory period "can do no significant violence to the central purpose of the securities laws," since the six-months requirement is essentially arbitrary (A-8). The authorities, however, emphasize the public policy requiring strict adherence to the mechanical rule imposed by § 16(b). In the leading case of Smolowe v. Delendo Corp., 136 F. 2d 231, 239 (2d Cir.), cert. denied, 320 U.S. 751 (1943), this Court held:

> "The statute is broadly remedial.*** [It] was intended to be thoroughgoing, to squeeze all possible profits out of stock transactions, and thus to establish a standard so high as to prevent any conflict between the selfish interest of a fiduciary officer, director, or stockholder and the faithful performance of his duty. *** The only rule whereby all possible profits can be surely recovered is that of lowest price in, highest price out - within six months - as applied by the district court."

Repeatedly we have been reminded that the strict enforcement of § 16(b) includes the meticulous observance of its time limits by corporate insiders; Champion Home Builders Co. v. Jeffress, 490 F. 2d 611, 619 (6th Cir.), cert. denied sub nom. Jeffress v. Kramer, 416 U.S. 986 (1974), quoting from Bershad v. McDonough, 428 F. 2d 693, 696 (7th Cir. 1970), cert. denied, 400 U.S. 992 (1971):

> "The thrust of the statutory scheme thus placed responsibility for meticulous observance of the provision upon the shoulders of the insider. He was deemed capable of structuring his dealings to avoid any possibility of taint and therefore must bear the risks of any inadvertent miscalculation."

The generosity of the Court below in shortening the statutory period cannot be reconciled with the strict enforcement to which the statute is entitled.

Section 16(b) must be "given the construction that best serves the congressional purpose of curbing short-swing speculations by corporate insiders"; Reliance Electric Co. v. Emerson Electric Co., 404 U.S. 418, 424 (1972). Accord: Schur v. Salzman, 365 F. Supp. 725, 731 (S.D.N.Y. 1973):

> "The courts, particularly in our circuit, have consistently interpreted the section [i.e., § 16(b)] in the broadest possible terms in order not to defeat its objectives, resolving all doubts and ambiguities against the insider." (Footnote omitted)

With these guidelines in mind, we consider the various factors bearing on the interpretation of § 16(b).

The context of the statute.

Section 16(b) provides that an insider must surrender his short-swing profits "irrespective of any intention" on his part to hold the securities purchased "for a period exceeding six months". This clause of the statute would be pointless unless Congress meant to prescribe a holding period measuring a full six months.

Judge Dimock, in Stella, disregarded this statutory language as "a mere referential inaccuracy" (132 F. Supp. at 104). This characterization, we submit, is a question-begging fallacy. Of course, the reference of the statute to "a period exceeding six months" would be inaccurate if it were already established that the holding period is only six months minus

two days. But that is the very proposition that must be established; and it cannot be established by reading only part of § 16(b) and ignoring the balance. It is "fundamental that a section of a statute should not be read in isolation from the context of the whole act, and that *** in interpreting legislation, 'we must not be guided by a single sentence or member of a sentence, but [should] look to the provisions of the whole law and to its object and policy'"; Richards v. United States, 369 U.S. 1, 11 (1962). If 16(b) is read as a whole, the intent of Congress to provide a full six months' holding period emerges clearly.

To ascribe a different purpose to Congress would be unnatural and opposed to common understanding. Granting Judge Gurfein's statement (A-8) that the six-months' requirement is "essentially arbitrary", how much more arbitrary would it be to provide a holding period of six months minus two days! A legislative body setting an arbitrary time will naturally choose a round figure. Six months is a round figure; and we simply cannot conceive of any reason why Congress should have selected a period as odd and unusual

as six months minus two days.

Judicial interpretation.

It is thus no wonder that this Court as well as others have time and again described the 16(b) period as comprising six months, not six months minus one or two days. Thus, B. T. Babbitt, Inc. v. Lachner, 332 F. 2d 255, 258 (2d Cir. 1964), held that a purchase of shares on November 5, 1958 and a sale on May 6, 1959 "exceeded six months - if only by one day". Similarly, Gratz v. Claughton, 187 F. 2d 46, 52 (2d Cir.), cert. denied, 341 U.S. 920 (1951), held that a director or officer cannot safely buy and sell stock in his company "except at intervals of six months", and that an insider's sale can be matched by looking back and looking forward "for six months" for any purchase at a lower price. In Kornfeld v. Eaton, 327 F. 2d 263 (2d Cir. 1964), where an insider had purchased stock through exercise of an option, the plaintiffs emphasized that the statutory period was "less than six months" (brief for the plaintiffs-appellants, pp. 9, 18); this Court held, nevertheless, that "liability attaches

only where there is a purchase, pursuant to the exercise of an option, within six months of a sale" (p. 265). In none of these cases did this Court so much as hint that the statutory holding period might be a day or two less than six months from the initial purchase or sale.

The expressions of this Court have since been sanctioned by the Supreme Court. Kern County Land Co. v. Occidental Petroleum Corp., 411 U.S. 582, 595 (1973), said that liability under § 16(b) attaches -

> "for any profits realized from any purchase and sale or sale and purchase of stock occurring within a period of six months."

In Reliance Electric Co. v. Emerson Electric Co., 404 U.S. 418, 422 (1972), the Supreme Court said with respect to § 16(b):

> "A person avoids liability*** if he sells more than six months after purchase."

It may be true, as Judge Gurfein noted (A-8), that court and counsel in some of these cases did not give specific

consideration to the issue here involved; but that is no ground to brush the cases aside. Coming from the Supreme Court and this Court, repeated references to "six months" persuasively demonstrate that this is the natural and reasonable meaning of the statute, as it impresses itself on readers not given to the loose use of language. If that be true, it is a reasonable inference that the intent of Congress was the same.

Legislative materials.

Although the legislative materials bearing on the computation of the statutory period are less than ample, they all point in one direction.*

*As herein used, "House Hearings" refers to Stock Exchange Regulation, Hearing on H.R. 7852 and H.R. 8720 before the Committee on Interstate and Foreign Commerce, House of Representatives, 73d Cong., 2d Sess. (1934).

"Senate Hearings" refers to Stock Exchange Practices. Hearings on S. Res. 84 (72d Cong.), S. Res. 56 and 97 (73d Cong.) before the Committee on Banking and Currency, United States Senate, 73d Cong., 1st and 2d Sess. (1934).

Thomas Corcoran and Ferdinand Pecora were among the principal draftsmen of the bills that evolved into the Exchange Act (House Hearings 82-84; Senate Hearings 6463-65, 7703). Both men testified extensively. Mr. Pecora explained that an insider is permitted to profit from investments in his company -

> "provided his transactions are more than 6 months apart. *** If he buys and does not sell again for another 6 months, he does not have to account." (Senate Hearings 7742).

In the same vein, Mr. Corcoran stated that § 15 of the bill (H.R. 7852, the precursor of the present § 16) forbade an insider -

> "to carry on any short-term speculations in the stock. He cannot, with his inside information, get in and out of stock within six months. If he does, the profit goes to his company." (House Hearings 133).

Both explanations made it clear that the holding period was to be six months; neither suggested a diminution of the period by one or two days.

On April 17, 1934, a Senate Committee Report, S. Rep. 792, 73d Cong. 2d Sess., recommended the enactment of a bill, S.3420, providing for a holding period of "less than six months". The Report (pp. 20-21) stated that the bill called for the surrender of insider profits -

> "derived from sales and purchases within a period of 6 months or less." (emphasis added).

Against this legislative background, it would seem clear that Congress understood the statute to provide for a full six months' holding period.

Interpretation by the SEC.

In the construction of § 16(b), the views of the SEC, as the agency charged with the administration of the statute, are, of course, entitled to great deference; Udall v. Tallman, 380 U.S. 1, 16 (1965). The Commission clearly considers the applicable period to be six full months, not one or two days less. SEC Rule 16b-6, 17 CFR 240.16b-6 (quoted in pertinent part in the Addendum, p.31 below),

deals with insider profits arising from the exercise of stock options and a corresponding stock sale; the Rule is designed to hold the insider liable only for his short-swing profit, not for the long-term appreciation of the option. Sec. Exch. Act Release No. 4509, '48-'52 CCH Fed. Sec. L. Rep. ¶ 76,080 (1950). Significantly, the Rule denominates the short-swing period as "within six months before or after the date of sale"; Rule 16b-6(b). The Commission thus treated the short-swing period as "a period of six full months ending at midnight on the day of sale"; Morales v. Walt Disney Productions, 361 F. Supp. 1157, 1158 (S.D.N.Y. 1973). The same view is repeatedly expressed in the Commission's Release, supra:

> "Accordingly, under Section 16(b) the insider who has held his investment for six months is free to realize what he can from selling it." (pp. 78,756-57; emphasis added).
>
> "***the critical period for measuring short swing aspects of profit derived from the exercise of an option is the six months after the sale." (p. 78,758; emphasis added).

In sum, all relevant factors - the context of § 16(b), its reasonable meaning, its legislative history, and the great weight of its judicial and administrative interpretation - point to a statutory period of a full six months. Under familiar rules governing the computation of time, the day of the initial securities purchase (or sale) is excluded from the six months, whereas the last day of the six months is included. But even if only one of these two propositions be sustained, defendants sold and bought within the statutory period, so that they are accountable for their profits.

CONCLUSION

The order below should be reversed and the case remanded for further proceedings.

Respectfully submitted,

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Dated: December 9, 1974

ADDENDUM

Section 16(a) and (b) of the
Securities Exchange Act of 1934,
15 USC § 78p(a) and (b).

Sec. 16. (a) Every person who is directly or indirectly the beneficial owner of more than 10 per centum of any class of any equity security (other than an exempted security) which is registered pursuant to section 12 of this title, or who is a director or an officer of the issuer of such security, shall file, at the time of the registration of such security on a national securities exchange or by the effective date of a registration statement filed pursuant to section 12(g) of this title, or within ten days after he becomes such beneficial owner, director or officer, a statement with the Commission (and, if such security is registered on a national securities exchange, also with the exchange) of the amount of all equity securities of such issuer of which he is the beneficial owner, and within ten days after the close of each calendar month thereafter, if there has been a change in such ownership during such

month, shall file with the Commission (and if such security is registered on a national securities exchange, shall also file with the exchange), a statement indicating his ownership at the close of the calendar month and such changes in his ownership as have occurred during such calendar month.

(b) For the purpose of preventing the unfair use of information which may have been obtained by such beneficial owner, director, or officer by reason of his relationship to the issuer, any profit realized by him from any purchase and sale, or any sale and purchase, of any equity security of such issuer (other than an exempted security) within any period of less than six months, unless such security was acquired in good faith in connection with a debt previously contracted, shall inure to and be recoverable by the issuer, irrespective of any intention on the part of such beneficial owner, director, or officer in entering into such transaction of holding the security purchased or of not repurchasing the security sold for a period exceeding six months. Suit to recover such profit may be instituted at law or in equity

in any court of competent jurisdiction by the issuer, or by the owner of any security of the issuer in the name and in behalf of the issuer if the issuer shall fail or refuse to bring such suit within sixty days after request or shall fail diligently to prosecute the same thereafter; but no such suit shall be brought more than two years after the date such profit was realized. This subsection shall not be construed to cover any transaction where such beneficial owner was not such both at the time of the purchase and sale, or the sale and purchase, of the security involved, or any transaction or transactions which the Commission by rules and regulations may exempt as not comprehended within the purpose of this subsection.

Rule 16b-6(a) and (b) of
the Securities and Exchange Commission,
17 CFR 240.16b-6(a) and (b).

Rule 16b-6. Exemption of Long Term Profits Incident to Sales Within Six Months of the Exercise of an Option.

(a) To the extent specified in paragraph (b) of this rule the Commission hereby exempts as not comprehended within

the purposes of section 16(b) of the Act any transaction or transactions involving the purchase and sale or sale and purchase of any equity security where such purchase is pursuant to the exercise of an option or similar right either (1) acquired more than six months before its exercise, or (2) acquired pursuant to the terms of an employment contract entered into more than six months before its exercise.

(b) In respect of transactions specified in paragraph (a) the profits inuring to the issuer shall not exceed the difference between the proceeds of sale and the lowest market price of any security of the same class within six months before or after the date of sale. Nothing in this rule shall be deemed to enlarge the amount of profit which would inure to the issuer in the absence of this rule.

APPENDIX

UNITED STATES COURT OF APPEALS
for the Second Circuit

Docket No. 74-2280

COLONIAL REALTY CORPORATION,
Plaintiff-Appellant,
against
JOHN MacWILLIAMS, JR., JAMES E. BRENNAN
and COLONIAL PENN GROUP, INC.,
Defendants-Appellees.

On Appeal from the United States District Court
for the Southern District of New York

JOINT APPENDIX

POMERANTZ LEVY HAUDEK & BLOCK
295 Madison Avenue
New York, New York 10017
Attorneys for Plaintiff-Appellant

PAUL, WEISS, RIFKIND, WHARTON & GARRISON
345 Park Avenue
New York, New York 10022
Attorneys for Defendants-Appellees
John MacWilliams, Jr. and
James E. Brennan

GOLD, FARRELL & MARKS
595 Madison Avenue
New York, New York 10022
Attorneys for Defendant-Appellee
Colonial Penn Group, Inc.

JOINT APPENDIX TO BRIEF

TABLE OF CONTENTS

DOCKET ENTRIES

COLONIAL REALTY CORP. V. JOHN MacWILLIAMS, JR. ET AL.

74 CIV. 1818

74 C.I.V. 1818

DATE	PROCEEDINGS
Apr-25-74	Filed Complaint and issue summons.
May 6-74	Filed summons and Marshals return - served: Colonial Penn Group by A.A. Leban on 4-30-74 John McWilliams, Jr. on 4-30-74 by A.A. Leban James E. Brennan on 4-30-74
May-20-74	Filed deft. MacWilliams and J.E. Brennan's notice of motion to dismiss pursuant to Rule 12(b)(6) - ret. 5-31-74
May-20-74	Filed memorandum of law by defendants MacWilliams and Brennan in support of motion to dismiss.
May 22-74	Filed stip. and order that the time of deft. Colonial Penn Group Inc. to answer complaint is ext. to June 10,1974. So ordered, Gurfein,J.
Jun- 3-74	Filed stip. and order that the motion to dismiss is adj. to 6-14 and that pltf. will serve its brief in opposition by 6-10. Carter, J.
Jun-11-74	Filed stip. and order that motion to dismiss is adj. to 6-20-74 that pltf. will serve brief in opposition by June 14-74 -- G.
Jun-14-74	Filed stip. and order that the time of deft. Colonial Penn Group to answer is ext. to a date ten days after the entry of an order disposing of the motion by deft. MacWilliams and Brennan to dismiss. -- Gurfein, J.
Jun-17-74	Filed pltf's memorandum of law in opposition to motion to dismiss
Jun-20-74	Filed reply memorandum of deft. MacWilliams and Brennan in support of motion to dismiss.
Aug-22-74	Filed OPINION #41106..that defendants motion to dismiss is granted and the complaint is dismissed. So ordered. - Gurfein, J. (for failure to state a claim)
Sep-11-74	Filed order that defendants' motion to dismiss the complaint is granted, that the complaint is dismissed on the merits as to defendants and that the Clerk is directed forthwith to enter judgment accordingly.- Judgment entered, Clerk on 9-25-74.
Sep-19-74	Filed pltf's notice of appeal to the USCA for the 2nd Circuit from opinion #41106 and order filed 9-11-74 - copies mailed to Paul Weiss Goldberg Rifkind Wharton & Garrison, Esqs. and Gold Farrell & Marks, Esqs.
Oct-23-74	Filed notice that record on appeal has been transmitted to the U.S.C.A.

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

- -x

COLONIAL REALTY CORPORATION,

Plaintiff,

-against-

JOHN MacWILLIAMS, JR., JAMES E. BRENNAN and COLONIAL PENN GROUP, INC.,

Defendants.

- -x

COMPLAINT

Plaintiff, by its attorneys, Pomerantz Levy Haudek & Block, for its complaint alleges upon information and belief, except for ¶¶ 2(a), 2(b) and 2(c), which are alleged upon knowledge:

1. This action arises under the Securities Exchange Act of 1934, as amended, 15 USC §§ 78a et seq. (the "Act"), and in particular, § 16(b) thereof, 15 USC § 78p(b). The jurisdiction of this Court is based upon the Act and, in particular, § 27 thereof, 15 USC § 78aa.

2. (a) Plaintiff is the owner of common stock of defendant Colonial Penn Group, Inc. ("Penn Group") and has been such continously since November 1971 and at the time of the wrongs complained of herein.

(b) Plaintiff brings this action derivatively on behalf of Penn Group.

(c) This action is not brought collusively to confer upon this Court jurisdiction which it otherwise would not have.

3. Penn Group is a Delaware corporation, incorporated in 1963. The outstanding common stock of Penn Group is and at all times relevant herein has been listed on the New York Stock Exchange and registered pursuant to § 12 of the Act.

4. Defendant MacWilliams is now and was at all relevant times an officer and director of Penn Group, specifically the Chief Executive Officer and Chairman of the Board of Directors.

5. Defendant Brennan is now and was at all relevant times an officer of Penn Group, specifically senior vice president and treasurer.

6. Defendant MacWilliams sold 50,000 shares of Penn Group's common stock in the open market at $63.49 per share on December 20, 1972, and purchased 45,000 shares thereof by exercising an option at $6.86 per share on June 19, 1973.

7. Defendant Brennan sold 4,000 shares of Penn Group's common stock in the open market at $62.13 per share on December 22, 1972, and purchased 5,000 shares thereof by exercising an option at $12.00 per share on June 21, 1973.

8. As a result of the foregoing, defendants MacWilliams and Brennan are each liable to Penn Group pursuant to § 16(b) of the Act for their profits in the sale and purchase of Penn Group's equity securities within a period of less than six months.

9. Two years have not elapsed since such profits were realized by the individual defendants.

10. On February 22, 1974, plaintiff, through its attorneys, made demand on Penn Group and its board of directors to bring this suit, but they have failed or refused to sue.

WHEREFORE, plaintiff prays for judgment:

A. Requiring MacWilliams and Brennan to pay over to Penn Group all the profits they made on their sales and purchases of Penn Group's equity securities within a period of less than six months;

B. Awarding plaintiff the costs and expenses of this action including reasonable counsel fees; and

C. Granting such other and further relief as may be just.

Dated: New York, New York
April 25, 1974.

POMERANTZ LEVY HAUDEK & BLOCK

By: Richard M Meyer
A Member of the Firm

Attorneys for Plaintiff
295 Madison Avenue
New York, New York 10017
(212) 532-4800

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

- -x

COLONIAL REALTY CORPORATION, :

Plaintiff, :

-against- : 74 Civ. 1818 (MIG)

JOHN MacWILLIAMS, JR., JAMES E. BRENNAN and COLONIAL PENN GROUP, INC., : NOTICE OF MOTION

Defendants. :

- -x

S I R S :

PLEASE TAKE NOTICE that upon the complaint herein, the undersigned will move this Court, before the Honorable Murray I. Gurfein, District Judge, on May 31, 1974 at 10:00 o'clock A.M. or as soon thereafter as counsel can be heard, for an order pursuant to Rule 12(b)(6) of the Federal Rules of Civil Procedure dismissing the complaint for failure to state a claim upon which relief can be granted.

Dated: New York, New York
May 20, 1974

Yours etc.,

PAUL, WEISS, RIFKIND, WHARTON & GARRISON

By _____

Attorneys for Defendants
John J. MacWilliams, Jr., and
James E. Brennan
345 Park Avenue
New York, New York 10022
Tel: (212) 935-8000

TO: POMERANTZ LEVY HAUDEK & BLOCK
Attorneys for Plaintiff
295 Madison Avenue
New York, New York 10017

GOLD, FARRELL & MARKS
Attorneys for Defendant
Colonial Penn Group, Inc.
595 Madison Avenue
New York, New York 10022

OPINION OF GURFEIN, D. J.

1. Securities Regulation ⇐111

Sale of stock by one corporate officer on December 20 and purchase of shares in the corporation on the following June 19 and sale by second corporate officer on December 22 and purchase on the following June 21, did not constitute short-swing sales within a period of "less than six months." Securities Exchange Act of 1934, § 16(b), 15 U.S.C.A. § 78p(b).

See publication Words and Phrases for other judicial constructions and definitions.

2. Courts ⇐96(7)

Although stare decisis is not so rigid as to require perpetuation of error, decision that phrase "less than six months" as applied to short-swing stock transactions does not include the date of sale was not so clearly in error as to require reconsideration. Securities Exchange Act of 1934, § 16(b), 15 U.S.C.A. § 78p(b).

3. Courts ⇐96(7)

Absent a showing of significant unworkability or injustice, determination of method of computing six-month period set out in statute which prohibits the unfair use of information obtained by insiders on short-swing sales was one on which investors had a right to rely. Securities Exchange Act of 1934, § 16(b), 15 U.S.C.A. § 78p(b).

COLONIAL REALTY CORPORATION, Plaintiff,

v.

John MacWILLIAMS, Jr., et al., Defendants.

No. 74 Civ. 1818.

United States District Court, S. D. New York.

Aug. 21, 1974.

Shareholder's derivative action was brought against two corporate officers. On corporate officer's motion to dismiss, the District Court, Gurfein, J., held that sale of stock on December 20 and repurchase of stock on the following June 19th by one officer and sale on December 22nd and repurchase on June 21st by second officer did not occur within periods of less than six months for purposes of statute prohibiting unfair use of information obtained by insiders on short-swing sales.

Motion to dismiss granted.

Pomerantz Levy Haudek & Block, New York City, for plaintiff.

Paul, Weiss, Rifkind, Wharton & Garrison, New York City, for defendants.

GURFEIN, District Judge:

This is a shareholder's derivative action brought by plaintiff in the name of Colonial Realty Corporation (Colonial) against two officers of Colonial Penn Group, Inc. (CPG). The complaint alleges that defendants MacWilliams (chief executive officer and chairman of

CPG's board of directors) and Brennan (CPG's senior vice president and treasurer) are liable to CPG pursuant to § 16(b) of the Securities Act of 1934, 15 U.S.C. § 78p(b) for profits realized in their short-swing sale and purchase of certain CPG securities. CPG has been joined as party defendant because of its failure to bring this action upon plaintiff's demand.

[1] Defendants MacWilliams and Brennan now move pursuant to Fed.R. Civ.P. 12(b)(6) to dismiss the complaint for failure to state a claim upon which relief can be granted. The sole issue raised by their motion is whether the transactions complained of occurred within the statutory period of "less than six months." For the reasons stated below I conclude that they did not, and the motion to dismiss will therefore be granted.

The complaint establishes the following facts for purposes of this motion:

> "6. Defendant MacWilliams sold 50,000 shares of Penn Group's common stock in the open market at $63.49 per share on December 20, 1972, and purchased 45,000 shares thereof by exercising an option at $6.86 per share on June 19, 1973.
>
> "7. Defendant Brennan sold 4,000 shares of Penn Group's common stock in the open market at $62.13 per share on December 22, 1972, and purchased 5,000 shares thereof by exercising an option at $12.00 per share on June 21, 1973."

The relevant portion of section 16(b) provides:

> "(b) For the purpose of preventing the unfair use of information which may have been obtained by such beneficial owner, director, or officer by reason of his relationship to the issuer, any profit realized by him from any purchase and sale, or any sale and purchase, of any equity security of such issuer (other than an exempted security) *within any period of less than six months*, * * * shall inure to and be recoverable by the issuer, irrespective of any intention on the part of such beneficial owner, director, or officer in entering into such transaction of holding the security purchased or of not repurchasing the security sold for a period exceeding six months. * * *" (Emphasis supplied.)

Plaintiff contends that a purchase of securities on the final day of a six-month period beginning with the date of a previous sale falls within this statutory scheme. This argument admittedly requests the court to overturn a rule established in this circuit some nineteen years ago in Stella v. Graham-Paige Motors Corp., 132 F.Supp. 100 (S.D.N.Y. 1955), remanded on other grounds, 232 F.2d 299 (2d Cir.), cert. denied, 352 U.S. 831, 77 S.Ct. 46, 1 L.Ed.2d 52 (1956).

In *Stella* the District Court interpreted the phrase "within a period of less than six months" as follows:

> ". . . Graham-Paige [the defendant] construes the words 'period of less than six months' to mean a period the first and last days of which each include the twenty-four hours from midnight to midnight, and the last day of which is the second day prior to the date corresponding numerically to that of the first day of the period in the sixth succeeding month. For example, the period from and including January 1st to and including June 29th would be a 'period of less than six months' but the period to and including June 30th would be a period of exactly six months. Thus profit realized from a purchase on January 1st and a sale on June 30th would not be recoverable under the statute.
>
> "That construction is correct." 132 F.Supp. at 103–104.

The Court of Appeals approved this formulation in the following language: "We agree with the trial judge that the purchase of the stock occurred on Feb-

ruary 10, 1947, and that therefore sales made *before* August 8, 1947, were within the statutory period." 232 F.2d at 301 (Emphasis supplied).

Clearly, if this formulation is accepted here plaintiff's claim must fail, since the sale/purchase dates of both MacWilliams' and Brennan's transactions (Dec. 20/June 19 and Dec. 22/June 21, respectively) are patterned exactly after the formulation in *Stella*.

Plaintiff contends, however, that both courts were in error in that formulation because they included the initial purchase or sale date in measurement of the six-month period and because they took literally the statute's "less than" wording without giving adequate attention to the rest of the passage in which that phrase appears.

Although I might have accepted these arguments had I, rather than the Court of Appeals in *Stella*, approached this problem in the first instance, I now feel constrained by the doctrine of *stare decisis* to follow the rule established almost nineteen years ago.

[2] While plaintiff is certainly correct in asserting that *stare decisis* is not so rigid as to require perpetuation of error, I cannot agree that this is the kind of situation in which overturning an established principle is appropriate or desirable. Most importantly, the *Stella* formulation is by no means clearly in error.

Nor does the *Stella* rule suffer from any other deficiencies which might persuade me to reexamine it. On a practical basis, it has not proved unworkably difficult to apply. Further, since the six-month requirement it implements is itself an essentially arbitrary legislative guidepost, the *Stella* approach can do no significant violence to the central purpose of the securities laws.

Finally, I am unimpressed by the authorities plaintiff has assembled in support of its position. Plaintiff cites a number of passing judicial references to the § 16(b) six-month requirement which by labored inference might have some relevance, but none of which contains any indication that the courts or counsel in those cases gave direct consideration to this issue. Similarly, the analogies plaintiff attempts to draw to methods of time measurement in unrelated areas of law, in an apparent appeal to the need for uniformity in the system as a whole, are at best of minimal impact.

[3] I conclude that the central values underlying the doctrine of *stare decisis*—the interests of the legal system in consistency and uniformity—are fully applicable and dispositive of this issue. The *Stella* rule has been cited by virtually every important research source which might be consulted by a corporate insider in planning dealings in his company's securities under § 16(b), and no contrary authority has been presented.[1] Under such circumstances, absent a showing of significant unworkability or injustice, I must agree with defendants that they and other investors had a right to rely on an established rule of this circuit.

The motion to dismiss is therefore granted and the complaint dismissed. So ordered.

1. See, e. g., 15 U.S.C.A. § 78p(b) n. 56 (1971); 2 L. Loss, Securities Regulation 1058 (2d Ed. 1961) and 5 L. Loss, Securities Regulation 3021-22 (1969 Supp.); 2 CCH Fed.Sec.L.Rep. ¶¶ 26,101.012, 26,101.60 (1973); R. Jennings and H. Marsh, Securities Regulation 1307 (3d Ed. 1972). Nor, incidentally, have I been able to discover any movement by Congress or by the Securities Exchange Commission during the 19 years since *Stella* to change the effect of its rule. — Compare the approach of Judge Bonsal interpreting SEC rule 16b-6 for purposes of *calculating profits* due when improper short-swing transactions have been discovered. Morales v. Walt Disney Productions, 361 F.Supp. 1157 (S.D.N.Y.1973).

ORDER DISMISSING COMPLAINT

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

COLONIAL REALTY CORPORATION,

Plaintiff,

-against-

JOHN MacWILLIAMS, JR., JAMES F. BRENNAN and COLONIAL PENN GROUP, INC.,

Defendants.

74 Civ. 1818 (WHG)

ORDER

Defendants John J. MacWilliams, Jr. and James E. Brennan having moved pursuant to Fed. R. Civ. P. 12(b)(6) for an order dismissing the complaint for failure to state a claim upon which relief may be granted; and the Court having considered memoranda in support of and in opposition to the motion, and after due deliberation having found for the reasons stated in its Memorandum and Order dated August 21, 1974 that defendants are entitled to an order dismissing the complaint on the merits as to all defendants,

NOW, upon the motion of Paul, Weiss, Rifkind, Wharton & Garrison, it is

ORDERED that defendants' motion to dismiss the complaint is granted, that the complaint is dismissed on the merits as to all defendants and that the Clerk is directed to enter judgment accordingly.

Dated: New York, New York
September 5, 1974

U. S. D. J.

ORDER DISMISSING COMPLAINT

APPROVED AS TO FORM OF ORDER:

POMERANTZ LEVY HAUDEK & BLOCK

By Richard M Meyers
Attorneys for Plaintiff

GOLD, FARRELL & MARKS

By
Attorneys for Defendant
Colonial Penn Group, Inc.

PAUL, WEISS, RIFKIND, WHARTON & GARRISON

By Richard Wharton
Attorneys for Defendants
MacWilliams and Brennan

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

- -x

COLONIAL REALTY CORPORATION, :

Plaintiff, :

-against- : 74 Civ. 1818 (MIG)

JOHN MacWILLIAMS, JR., JAMES E. BRENNAN and COLONIAL PENN GROUP, INC., : NOTICE OF APPEAL

Defendants. :

- -x

S I R S :

Notice is hereby given that Colonial Realty Corporation, plaintiff above named, hereby appeals to the United States Court of Appeals for the Second Circuit from the order dismissing the complaint, entered in this action on the 22nd day of August 1974, and the subsequent order of dismissal entered on or about the 5th day of September 1974.

Dated: New York, New York
September 19, 1974

Yours, etc.,

POMERANTZ LEVY HAUDEK & BLOCK

By: Richard M. Meyer
Attorneys for Plaintiff
295 Madison Avenue
New York, New York 10017
(212) 532-4800

TO: PAUL, WEISS, GOLDBERG,
RIFKIND, WHARTON & GARRISON, ESQS.
345 Park Avenue
New York, N. Y.

GOLD, FARRELL & MARKS, ESQS.
595 Madison Avenue
New York, N. Y. 10022

Service of ~~three (3)~~ Two (2) copies of the within
Briefs Joint Appendix is hereby admitted
this 9th day of December, 1974

.....

Attorney(s) for

(2) COPY RECEIVED
12-9 19 74
PAUL, WEISS, RIFKIND, WHARTON & GARRISON
By Clorice A Lauro

Service of ~~three (3)~~ Two (2) copies of the within
Briefs Joint Appendix is hereby admitted
this 9th day of December, 1974

.....

Attorney(s) for

COPY RECEIVED
December 9, 1974
GOLD, MARSHALL & MARKS
BY J Feller